

## Chapter 1 : Introduction

### 1.1 Background

A new mode of central excise taxation procedure called Modvat (Modified Value Added Tax) was introduced from 1 March 1986 to implement one of the measures contemplated in the long term fiscal policy announced by the Government in December 1985.

The scheme enables manufacturers to avail credit of duty paid on the inputs (from the year 1986) and capital goods (from the year 1994) and utilise such credit for payment of duty on the final products manufactured by them. The scheme was renamed as Cenvat Credit Scheme with effect from 1 April 2000. This was replaced by Cenvat Credit Rules, 2001 effective from 1 July 2001 which simplified Cenvat provisions and procedures for allowing credit of duty paid on specified inputs and capital goods used in or in relation to the manufacturer of specified final products. Further revision the rules were made through Cenvat Credit Rules, 2002 with effect from 1 March 2002.

The Central Government introduced the levy of tax on services from the year 1994. With amendment to Section 94(2) of Finance Act, 1994 in the year 2002, giving powers to Central Government to make rules relating to credit of Service Tax (ST). Central Government introduced Service Tax Credit Rules, 2002 with effect from 16 August 2002. This scheme was similar to Cenvat scheme on excise but was limited only to credit on input service used in providing taxable output services. Cenvat Credit Rules, 2004, have been introduced and made effective from 10 September 2004 so that credit of input duties and tax can be extended across goods and services.

### 1.2 Organisational set up

Central Board of Excise and Customs (CBEC) set up under the Central Boards of Revenue Act, 1963 is a part of the Department of Revenue under the Ministry of Finance, Government of India. It deals with the tasks of formulation of policy concerning levy and collection of Customs, Central Excise duties and Service Tax, prevention of smuggling and administration of matters relating to Customs, Central Excise, Service Tax and Narcotics. The Board is the administrative authority for its subordinate organisations, including Custom Houses, Central Excise and Service Tax Commissionerates and the Central Revenues Control Laboratory.

### 1.3 Legal provisions

**1.3.1** Section 37 of Central Excise Act, 1944, empowers the Central Government to make rules inter alia to:

- (i) provide for the credit of duty paid or deemed to have been paid on the goods used in or in relation to the manufacture of excisable goods;
- (ii) provide for credit of service tax leviable under Chapter V of Finance Act, 1994 paid or payable on taxable services used in, or in relation to, the manufacture of excisable goods;
- (iii) provide for the giving of credit of sums of money with respect to the raw materials used in the manufacture of excisable goods.

**1.3.2** Section 94 of the Finance Act, 1994, empowers the Central Government to make rules for credit of service tax paid on the services consumed or duties paid or deemed to have been paid on goods used for providing a taxable service.

### 1.4 Utilisation of Cenvat credit for payment of duty

In the scheme of availing Cenvat credit and utilising it for payment of duty/tax, payment from Cenvat credit represents duty/tax already paid on inputs and input services used in the manufacture of goods or provision of service. Table 1 shows trend of Central Excise (CE) collections through Personal Ledger Account (PLA) and Cenvat credit during the period of review.

**Table 1: Trend of central excise collection through PLA and Cenvat credit for period 2012-13 to 2014-15**

(₹ in crore)

Year	No. of assessees	CE duty paid through PLA		CE duty paid through Cenvat credit		CE duty paid from Cenvat credit as % of PLA payments
		Amount	% change over previous year	Amount	% change over previous year	
2012-13	4,09,139	1,75,845	--	2,58,697	--	147.12
2013-14	4,35,213	1,69,455	-3.63	2,73,323	5.65	161.30
2014-15	4,67,286	1,89,038	11.56	2,91,694	6.72	154.30

Source : Figures furnished by the Ministry.

Table 2 shows trend of service tax collections through PLA (cash) and Cenvat credit during the period of review.

**Table 2: Trend of service tax collection through PLA and Cenvat credit for period 2012-13 to 2014-15**

(₹ in crore)

Year	No. of assessees	Service tax paid through PLA		Service Tax paid through Cenvat credit		ST paid from Cenvat credit as % of PLA payments
		Amount	% change over previous year	Amount	% change over previous year	
2012-13	19,82,297	1,32,601	--	5,507	--	4.15
2013-14	22,58,599	1,54,780	16.72	15,090	174.01	9.74
2014-15	25,11,728	1,67,969	8.52	14,404	-4.54	8.57

Source : Figures furnished by the Ministry.

### 1.5 Why we chose this topic

Keeping in view significant amount of duty/tax paid through Cenvat in last three years, various changes in recent years such as restriction to take Cenvat credit within six months (from September 2014)/within one year (from March 2015) and a large number of cases of irregular availment/utilisation of Cenvat credit observed during our regular audit, it was felt necessary to evaluate the adequacy of the existing provisions and effectiveness of implementation and monitoring mechanisms.

### 1.6 Audit Objectives

The Performance Audit was conducted to seek assurance whether:

- a) provisions in the rules/clarifications/procedures as laid down are unambiguous and adequate to safeguard any misuse of the scheme;
- b) internal control and monitoring mechanism were in place and effective; and
- c) departmental administration was efficient in implementing and ensuring compliance with the rules and regulations as laid down in the Cenvat Credit Rules, 2004, and other related rules.

## 1.7 Scope of audit and coverage

We selected 20 per cent of Commissionerates/Divisions/Ranges (CDR) and all the five Large Taxpayer Unit (LTU) Commissionerates. While doing so the CDRs having maximum number of assessees paying duty more than ₹ one crore per annum through Cenvat credit were selected. Thus, we selected and covered 41<sup>1</sup> out of 145 Commissionerates, 68 out of 737 divisions, 129 out of 3,649 ranges and 469 out of 4,54,080 assessees from the selected Commissionerates. Within the selected CDRs all assessees paying duty/tax of more than ₹ three crore through Cenvat credit, 50 per cent assessees paying duty/tax amount of between ₹ one to three crore and 20 per cent assessees paying duty/tax amount of upto ₹ one crore through Cenvat credit per annum were selected. The period of examination of this performance audit is from 2012-13 to 2014-15.

## 1.8 Acknowledgement

We acknowledge the co-operation extended by Central Board of Excise and Customs (CBEC) and its subordinate formations, in providing the necessary records for the conduct of this audit.

We discussed the audit objectives and scope of the performance audit in an entry conference with CBEC officers on 28 April 2015 and exit conference was held on 4 March 2016. The Ministry furnished the reply in February and April 2016 which are included in this report.

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<sup>1</sup> Ahmedabad-III, Alwar, Bengaluru LTU, Bengaluru-I, Bharuch, Bhubaneswar-I, Bhubaneswar-II, Bilaspur, Bolpur, Chandigarh-I, Chennai LTU, Chennai-III, Dehradun, Delhi LTU, Delhi-I, Delhi-I ST, Faridabad-II, Ghaziabad, Guwahati, Gwalior, Hyderabad-III, Hyderabad-IV, Indore, Jaipur, Jamshedpur, Kochi, Kolkata LTU, Kolkata-I ST, Mumbai LTU, Noida ST, Noida-I, Patna, Pune-III, Raigad, Raipur, Ranchi, Silvasa, Mumbai-II ST, Mumbai-VII ST, Thane-I and Thiruvananthapuram